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In the Supreme Court of the United States

OCTOBER TERM, 1941

No. .....

FLORENCE H. EHRMAN,
Petitioner,
v.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

CLARA HELLMAN HELLER,
Petitioner,
v.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

FRANCES J. HELLMAN and WELLS FARGO BANK & UNION TRUST CO., Trustees under the Last Will and Testament of I. W. HELLMAN, JR., Deceased,
Petitioners,
v.
COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit

To the Honorable Harlan Fiske Stone, Chief Justice of the United States, and to the Associate Justices of the Supreme Court of the United States:

Your petitioners respectfully show:

I.

SUMMARY STATEMENT OF THE MATTER INVOLVED

This proceeding involves petitioners' Federal income taxes for the year 1935, the Commissioner of Internal Revenue having proposed to assess a deficiency against Florence H. Ehrman in the amount of $11,122.24 (Record, page 49), against Clara Hellman Heller in the amount of $7,177.79 (Record, page 50), and against Frances J. Hellman and Wells Fargo Bank & Union Trust Co., Trustees under the last will and testament of I. W. Hellman, Jr., deceased, in the amount of $9,602.02 (Record, page 51).

Each of the petitioners filed separate petitions with the United States Board of Tax Appeals. The cases before the Board were consolidated and a hearing was held on June 9, 1939, in San Francisco. Subsequently, the Board rendered its opinion (promulgated on March 22, 1940; 41 B. T. A. 652), adverse to the petitioners and sustaining the position of the Commissioner, thereafter, on May 25, 1940, entering its decision in each case in accordance with such opinion.

NOTE: The facts herein involved are not in dispute. They are incorporated at length in the Findings of Fact of the United States Board of Tax Appeals (Record, pages 25 to 40), and are stated in somewhat shorter form in the opinion of the Circuit Court of Appeals for the Ninth Circuit (Record, pages 157 to 163). Accordingly we will not unduly burden this petition by reference to the record in support of the Statement of Facts.

From these decisions petitioners filed their petitions for review, pursuant to sections 1001 to 1003 of the Revenue Act of 1926, as amended, by the Circuit Court of Appeals for the Ninth Circuit. That court, after consolidating the cases for record, briefing and hearing, rendered its opinion sustaining the Board of Tax Appeals on June 6, 1941, and gave its judgment affirming the Board on the same date. Petitioners seek herein to have such judgment reviewed by this Court.

I. W. Hellman, a California banker, died in the year 1920, leaving a substantial estate of real and personal property which was distributed in equal shares to petitioners. The estate so distributed included a considerable amount of cash, securities of substantial value, several ranches and other real property, improved and unimproved. Among the ranches was the Repetto, consisting of 1569.93 acres, located about five miles east of the City Hall of Los Angeles and outside the city limits. The Repetto Ranch was acquired by Mr. Hellman sometime between 1870 and 1880.

Except for the sale of one ranch in order to pay inheritance taxes and the sales involved in this proceeding, none of the real property distributed from the Hellman Estate has been sold. No particular effort was made to sell the Repetto Ranch. Offers were received and rejected by petitioners, who always opposed subdivision and wished to sell outright, the ranch being used as grazing land and for agricultural and horticultural purposes.

In 1929 a sale was made to the Ransom Corporation of approximately 800 acres, consisting of most of the level land. The sum of $250,000 was paid on account, and title was conveyed to a bank, as trustee, which executed a declaration of trust whereby the title to the property was held as security for the balance of the purchase price payable over a period of years. Exclusive of interest, the average per acre contract price was approximately $3500. In the year 1932 the Ransom Corporation experienced financial difficulties and after negotiations with petitioners the greater part of the original acreage held under the trust was returned to them. An amendment to the declaration of trust was executed as of May 16, 1932, prescribing the terms upon which part of the acreage was so released to petitioners and the remaining acreage retained under the declaration of trust. There were approximately 273 acres retained by the Ransom Corporation which in the year 1933 again defaulted. This time the Hellman heirs reacquired the remaining acreage by foreclosure and sale thereunder.

During the period the property was held by the Ransom Corporation its character changed, and when it was acquired under foreclosure it was subdivided property. Part of the property had been sold to purchasers, some of whom held deeds thereto and others contracts of sale. The Ransom Corporation obligated itself to grantees and purchasers to whom it had contracted to sell the property to make certain improvements, including the laying of streets and sidewalks, the supplying of utility services, light, power and

water, the planting of trees, and to keep the property in condition. The property acquired on foreclosure was subject to such conditions and to other obligations which had been incurred as a result of public improvements, directly or indirectly affecting the property, including an assessment district bond issue, a bonded indebtedness in the amount of $155,000 for the construction of a boulevard, drainage district assessments, and obligations to the extent of approximately $84,000 for past taxes. The property had been subdivided, with a subdivision map filed of record, and by virtue thereof it was taxed as lots and not as acreage.

After the foreclosure, petitioners were confronted with the problem of what to do with the property in the condition in which it was reacquired. Their agent, Mr. Henry W. Keller, a man experienced in the real estate business, investigated the matter and advised them that they carry on with the sale of the property through subdivision. He testified that in his opinion there was no other way for the petitioners to dispose of the property which had been subject to the Ransom Corporation transaction unless they gave it away to somebody (Record, page 109). Mr. Keller was engaged to buy back certain of the contracts and lots and, where possible, to restore the property to acreage. This was done with respect to two tracts, consisting of approximately 46 acres, which had been previously subdivided by the Ransom Corporation, and a new tract was opened up of approximately 40.16 acres, because in Mr. Keller's opinion and in accordance with his recommendations this would bring the sub-

divided areas of the property together more centrally and nearer to the business district.

Meanwhile, through Mr. Keller's recommendations petitioners engaged an agent, Hamilton Sales Corporation, with which they entered into a contract under date of February 19, 1934, whereunder Hamilton Sales Corporation was to dispose of the property through subdivision. It is in connection with sales by this corporation for the year 1935 that the question herein arises. The contract provided that no lot or parcel should be sold at a lesser price than shown on attached schedules, which were subject to change by the petitioners. The terms of sale could be modified only with their consent and they were to determine the conditions of deeds and contracts of sale. Hamilton Sales Corporation was to receive a certain percentage of the gross selling price as its commission. In the year 1934 120 lots were sold for a total sales price of $161,679.87; in the year 1935, 186 lots were sold for the aggregate sum of $230,170. The total acreage which had been subdivided by the Ransom Corporation was 237.18. After return of the two tracts to acreage and the opening of the new tract, petitioners had 231 acres in subdivision for sale under contract with Hamilton Sales Corporation. The number of lots in subdivision was approximately 1098.

The Commissioner of Internal Revenue determined, and the Board of Tax Appeals sustained such determination as did the Circuit Court of Appeals for the Ninth Circuit, that the sales in 1935 were of property

held by petitioners primarily for sale to customers in the ordinary course of their trade or business, and hence the gains from such sales were not capital gains within the meaning of the Revenue Act of 1934.

Petitioners Florence H. Ehrman and Clara Hellman Heller are housewives, as is Frances J. Hellman, one of the trustees under the I. W. Hellman, Jr. Trust, and not engaged in any business (unless the Commissioner's determination is correct); Wells Fargo Bank & Union Trust Co. is similarly not engaged in any business except that of banking nor in any business as trustee for the Hellman Trust. The four children of I. W. Hellman, Jr., beneficiaries of the trust, are, respectively, a housewife, two bankers and an investment banker. None of the petitioners, nor any of the I. W. Hellman, Jr. children, took any part in negotiating sales of the property.

II.

STATUTORY PROVISIONS SUSTAINING JURISDICTION

Jurisdiction to sustain this petition is found in Section 240(a) of the Judicial Code, as amended by Act of Congress February 13, 1925, Chapter 229, #1; 43 Stats. 938; U. S. C. A. Title 28, section 347.

III.

STATUTE INVOLVED

The statute herein involved is Revenue Act of 1934, Chapter 277, Section 117, 48 Stats. 680, U. S. C. A., Title 26, section 101, reading:

> "(a) General Rule.—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net income:
>
> * * * (rates)
>
> (b) Definition of Capital Assets.—For the purposes of this title, 'capital assets' means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business."

IV.

JUDGMENT OF THE CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

The judgment of the Circuit Court of Appeals for the Ninth Circuit, with respect to which this petition is brought, was given and entered on June 6, 1941, in proceedings numbered 9723 in said court (Record, page 164). No petition for rehearing was filed.

V.

QUESTIONS PRESENTED

The questions presented by this petition are:

(1) Whether the Circuit Court of Appeals for the Ninth Circuit unreasonably and improperly concluded that petitioners' gains were realized from the sales of property held by them primarily for sale to customers in the ordinary course of their trade or business and, therefore, were taxable as ordinary and not as capital gains. This question involves determination whether the court erred in deciding that the property was held primarily for sale, that the sales were made in the ordinary course of petitioners' business, that petitioners were engaged in business, and that the sales were not casual.

(2) Whether the Circuit Court of Appeals for the Ninth Circuit unreasonably and improperly concluded that, notwithstanding that the sales herein involved were only part of a liquidation forced upon petitioners, such sales were made in the ordinary course of petitioners' trade or business, within the meaning of section 117(b) of the Revenue Act of 1934.

VI.

REASONS RELIED UPON FOR ALLOWANCE OF WRIT

1. The judgment of the Circuit Court of Appeals for the Ninth Circuit in the instant matter is purportedly in accord with previous rulings of that Cir-

cuit (*Richards v. Commissioner,* 81 Fed.(2d) 369; *Welch v. Solomon,* 99 Fed.(2d) 41; *Commissioner v. Boeing,* 106 Fed.(2d) 305 (certiorari denied, 308 U. S. 619)), but is in direct conflict with the decisions, on similar facts and under similar statutory provisions, of the Second Circuit in *Phipps v. Commissioner,* 54 Fed.(2d) 469, and of the Sixth Circuit in *Pope v. Commissioner,* 77 Fed.(2d) 599. The Ninth Circuit has, therefore, rendered a decision which is in conflict with decisions of two other Circuit Courts of Appeals, on a subject matter, to wit, an important provision of the Federal income tax statutes, which is of real and outstanding importance and with respect to which uniformity in decisions of the Circuits is necessary in the interest both of the United States and taxpayers.

2. The judgment of the Circuit Court of Appeals for the Ninth Circuit in this case decides an important question of Federal law, which has not been but which should be settled by this Court, namely, as to what constitutes property held by a taxpayer primarily for sale to customers in the ordinary course of his trade or business, within the definition of "capital assets" as used in section 117 of the Revenue Act of 1934 and similar statutes.

(a) The judgment of the Circuit Court of Appeals for the Ninth Circuit herein involved is in conflict with the decision of this Court in *Morrissey v. Commissioner,* 296 U. S. 344, 80 L. ed. 263, determining that a liquidation is not a business in connection with certain provisions of the Revenue Acts;

(b) The judgment of the Circuit Court of Appeals for the Ninth Circuit herein involved is in conflict with the decision of this Court in *Higgins v. Commissioner,* 312 U. S. 212, 85 L. ed. 475, involving the definition of "trade or business" under certain other sections of the income tax statutes.

WHEREFORE, your petitioners pray that a writ of certiorari issue under the seal of this Court directed to the Circuit Court of Appeals for the Ninth Circuit, commanding said court to certify and send to this Court a full and complete transcript of the record and the proceedings of said Circuit Court of Appeals had in the case numbered and entitled on its docket "No. 9723, Florence H. Ehrman, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Clara Hellman Heller, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Frances J. Hellman and Wells Fargo Bank & Union Trust Co., Trustees under the last will and testament of I. W. Hellman, Jr., Deceased, Petitioner, vs. Commissioner of Internal Revenue, Respondent." to the end that this cause may be reviewed and determined by this Court, as provided by the statutes of the United States, and that the judgment herein of said Circuit Court of Appeals for the Ninth Circuit be reversed by this Court, and for such other and further relief as to this Court may seem proper.

Dated, San Francisco, California, August 28, 1941.

SIDNEY M. EHRMAN,
LLOYD W. DINKELSPIEL,
Counsel for Petitioners

PETITIONER'S

BRIEF

In the Supreme Court of the United States

OCTOBER TERM, 1941

No. .....

FLORENCE H. EHRMAN,
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COMMISSIONER OF INTERNAL REVENUE,
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CLARA HELLMAN HELLER,
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COMMISSIONER OF INTERNAL REVENUE,
Respondent.

FRANCES J. HELLMAN and WELLS FARGO BANK & UNION TRUST CO., Trustees under the Last Will and Testament of I. W. HELLMAN, JR., Deceased,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Brief in Support of Petition

I.

OPINIONS OF THE COURTS BELOW

The opinion of the United States Board of Tax Appeals, promulgated on March 22, 1940, is reported in 41 B. T. A. 652, and appears in the record herein at pages 24 to 48. The opinion of the Circuit Court of Appeals for the Ninth Circuit given and rendered on June 6, 1941, is reported in 120 Fed. (2d) 607, and appears in the record herein at pages 156 to 163.

II.

JURISDICTION

1. The date of the decision to be reviewed is June 6, 1941 (Record, page 163); judgment was entered thereon on the same date (Record, page 164). No petition for rehearing was filed.

2. The statutory provisions which sustain the jurisdiction of this Court are section 240(a) of the Judicial Code, as amended by Act of Congress February 13, 1925, Chapter 229, #1; 43 Stats. 938, U. S. C. A. Title 28, section 347. The three months' period for the filing of this petition, as prescribed by the same statute (Act of Congress February 13, 1925, Chapter 229, #8; 43 Stats. 940, U. S. C. A. Title 28, section 350), has not yet expired.

3. This case is brought to this Court because the Circuit Court of Appeals for the Ninth Circuit has in this matter rendered a decision (a) in conflict with

the decisions of the Circuit Court of Appeals for the Second Circuit (*Phipps v. Commissioner,* 54 Fed. (2d) 469), and for the Sixth Circuit (*Pope v. Commissioner,* 77 Fed. (2d) 599), and (b) presenting an important question of Federal law which has not been but should be settled by this Court, and which the Circuit Court of Appeals for the Ninth Circuit determined in a manner in conflict with analogous decisions of this Court in *Morrissey v. Commissioner,* 296 U. S. 344, 80 L. ed. 263, and *Higgins v. Commissioner,* 312 U. S. 212, 85 L. ed. 475.

III.

STATEMENT OF THE CASE

A statement of the case has been set forth in the Petition for Certiorari, paragraph numbered I thereof, pages 2 to 7, and such statement is hereby adopted and made a part of this brief.

IV.

SPECIFICATIONS OF ERROR

1. The Circuit Court of Appeals for the Ninth Circuit erred in concluding that petitioners' gains were realized from the sale of property held by them primarily for sale to customers in the ordinary course of their trade or business and, therefore, were taxable as ordinary and not as capital gains within

the provisions of section 117 of the Revenue Act of 1934.

2. The Circuit Court of Appeals for the Ninth Circuit erred in concluding that the property was held by petitioners primarily for sale, that the sales were made by them in the ordinary course of their trade or business, that petitioners were engaged in business, and that the sales were not casual.

3. The Circuit Court of Appeals for the Ninth Circuit erred in concluding that notwithstanding the sales herein involved were made only in the course of a liquidation forced upon petitioners, such sales were of property held by petitioners primarily for sale in the ordinary course of their trade or business within the meaning of section 117(b) of the Revenue Act of 1934.

V.

SUMMARY OF ARGUMENT

1. In concluding that the gains realized by petitioners were capital gains, the Circuit Court of Appeals for the Ninth Circuit has necessarily determined that the sales of real property owned by petitioners and sold through the method of a subdivision were sales of property held by them primarily for sale to customers in the ordinary course of their trade or business, within the meaning of section 117 of the Revenue Act of 1934.

(a) In this conclusion, the decision of the Ninth Circuit is in direct conflict with that of the Second

Circuit in *Phipps v. Commissioner,* 54 Fed. (2d) 469, and of the Sixth Circuit in *Pope v. Commissioner,* 77 Fed. (2d) 599, and such conflict requires the determination of this Court to effect a uniformity of decision.

(b) The decision of the Circuit Court of Appeals for the Ninth Circuit involves a construction of what constitutes "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business", as that phrase is used in the definition of "capital assets" in section 117(b) of the Revenue Act of 1934. This important question of Federal law has not heretofore been determined by this Court, although its decisions most closely analogous are favorable to petitioners' position herein.

2. The undisputed evidence clearly establishes that petitioners' property was not held by them primarily for sale, that the sales were not made in the ordinary course of any trade or business of petitioners, that petitioners were not, in fact, engaged in any business, and that the sales were, particularly in comparison with the total property holdings of petitioners and even in relationship to the property of the Repetto Ranch herein involved, casual and not sufficiently frequent to constitute a business.

3. The property from which the sales herein involved were made was recovered by petitioners through foreclosure proceedings, and its condition at that time was such as to permit of no other disposition than through the medium of subdivision. This constituted a liquidation of the property, forced upon

petitioners, not by their own voluntary act but by the condition in which the property was returned to them. Such liquidation is not "business" in the ordinary sense (*Morrissey v. Commissioner,* 296 U. S. 344, 85 L. ed. 475) or as used in the federal revenue acts.

VI.

ARGUMENT

1. **The Circuit Court of Appeals for the Ninth Circuit erred in concluding that petitioners' gains were realized from the sale of property held by them primarily for sale to customers in the ordinary course of their trade or business.**

The facts in this case, apart from the question of liquidation, involve the not very unusual situation of property owners possessing an estate of some considerable size, held by them for investment or, as here, for agricultural, horticultural and grazing purposes, and finding themselves using the property uneconomically in view of the encroachments of a growing community and the consequent increase in the carrying charges of taxes, improvements and the like. To permit of its disposal, the character of the property is changed, either voluntarily by the taxpayer or involuntarily as in the instant case, from argicultural to urban use, from acres to lots, and it becomes part of a subdivision for purposes of sale. With varying differences, this was the situation in and around the City of Los Angeles presented by the instant case, as well as that of *Richards v. Commissioner,* 81 Fed. (2d)

369; and *Welch v. Solomon,* 99 Fed. (2d) 41, all in the Ninth Circuit; *Phipps v. Commissioner,* 54 Fed. (2d) 469, in the Second Circuit; and *Pope v. Commissioner,* 77 Fed. (2d) 599, in the Sixth Circuit. The determination of the Ninth Circuit, as opposed to that of the other two Circuits, is that where the property is so disposed of by way of subdivision, the sales are of property held primarily for sale to customers in the ordinary course of the taxpayer's trade or business, within the exceptions to the definition of "capital assets" set forth in section 117(b) of the Revenue Act of 1934, and similar statutory provisions.

Without at this point arguing the merits of the position of the Court of the Ninth Circuit, we desire to emphasize that it is in direct conflict with the decisions of the two other Circuits; therefore that this petition should be granted.

It is difficult, if not impossible, to distinguish this case from *Phipps v. Commissioner* in the Second Circuit. There two brothers and a sister purchased a tract of land in Palm Beach, Florida; they took title in the name of an agent, had the tract surveyed, cleared, plotted into lots, ornamented with trees, and furnished with roads, water, sewers and electric lights. A price was fixed at which the lots might be sold and sales were made through brokers over a period of years. Profits were realized in 1924 and 1925, the years involved in the court's decision. The Commissioner held that the taxpayers were real estate dealers and that the profits realized from the sale of the

Florida property did not constitute capital gains under the provisions of section 208(b) of the Revenue Act of 1924. The Board sustained the Commissioner, holding that the gains were derived from sales of property "held by the taxpayer primarily for sale in the course of his trade or business." As in the instant case, petitioners argued they were not themselves engaged in business, had nothing to do with the sales, and were disposing merely of a capital asset.

The Circuit Court, in reversing the Board and the Commissioner, held that the sales were not of property held primarily for sale in the course of taxpayers' trade or business, stating at page 471:

> "While the purchases were made with the hope of profitable sales at some future time they do not seem to have been sufficiently frequent, or the activities sufficiently engrossing, to give the taxpayers the vocation of real estate dealers or operators in 1924 or 1925."

And making this further comment on the same page:

> "Persons with large incomes of course invest their surplus funds in something, and if, to diversify their holdings, they buy land, with the expectation of selling it when a good price is offered, such an expectation cannot, in our opinion, convert some sales of land that had been held for seven or eight years into a trade or business in real estate. There should be a greater continuity and larger absorption of time in such transactions to make the taxpayers more than investors."

The court further concluded that the taxpayers' supervision of their own investment was neither a "trade" nor "business".

The case of *Pope v. Commissioner* in the Sixth Circuit admittedly presents certain points of factual difference from the instant matter; it involved the question whether a director and officer of a corporation, a substantial stockholder, was actually engaged in the corporation's business. However, in its essentials and the proposition for which it is cited, the case presents the same question as that involving the petitioners herein. The court stated the issue to be:

> "The sole question presented on this review is whether the evidence is legally sufficient to sustain the Board's finding that the lands were held by petitioners primarily for sale in the course of their trade or business." (page 600)

The land had been purchased in large tracts and subsequently subdivided for purposes of sale. Such disposal of the property was held not to constitute a business of the taxpayers, the court stating at page 600:

> "We think the purchase of the land is to be treated as an investment, and the investment having been made, the sale through real estate brokers is to be regarded as a conversion of capital assets and not a sale by the petitioners in the course of a trade or business."

It is true that the case of *Commissioner v. Boeing*, 106 Fed.(2d) 305 (CCA 9th), involves a somewhat

analogous situation to that herein (the transactions in the cited case were logging operations and not the sale of lots) and that a petition for certiorari was denied by this Court (308 U. S. 619, 84 L. ed. 517). An examination of the petition and supporting brief, however, discloses that the direct conflict between the decisions of the Ninth Circuit and those of the Second and Sixth Circuits, as evidenced by *Phipps v. Commissioner* and *Pope v. Commissioner,* was not precisely presented to this Court (although the cases last mentioned were cited), petitioners having relied upon a number of contentions in support of their application for a writ.

2. The Circuit Court of Appeals for the Ninth Circuit erred in concluding that petitioners were engaged in a business, that the property was held primarily for sale in the course of such business, and that the sales were not casual.

The rationale of the Circuit Court's determination that petitioners were engaged in business is that acting through an agent they sold in small lots by way of subdivision part of what had admittedly been investment property held in petitioners' family since prior to 1880; that through such sales the character of the property changed from an investment to a business; that in selling a capital asset, in the only manner available for its disposition, petitioners themselves changed from investors to people in business. Such determination is actually in conflict with the fairly recent decision of this Court in the case of *Higgins v. Commissioner,* 312 U. S. 212, 85 L. ed. 475, wherein

the management of a $35,000,000 estate was held not to be sufficiently a business to warrant the taxpayer in taking business deductions.

The property (the sales were of but a small part of the Repetto Ranch) was undoubtedly investment property held over the years and not "primarily for sale". When the subdivision was forced upon petitioners it is true that a sale of that small part of the property was petitioners' objective; but under the amendments to section 117(b) appearing for the first time in the Revenue Act of 1934, it is necessary not only that the property be held for sale in the course of petitioners' business but in the "ordinary" course and for sale "to customers". The Circuit Court refused to give effect to the 1934 amendments and concluded:

> "If, as we have held the fact to be here, the taxpayers were in the 'trade or business' of real estate subdivision, then certainly the sales of lots were to 'customers' in the 'ordinary' course of that business." (Record, page 163)

This conclusion does not necessarily follow. It is, indeed, difficult to find that these petitioners, with their other interests and varied property holdings, were selling lots to customers in the ordinary course of their trade or business. The words "to customers" and "ordinary", added by the 1934 amendments, must necessarily be construed as having a limiting effect upon the previous language of the section.

Petitioners urged before the Circuit Court that the sales were casual; the court denied this contention. On this issue there is very evidently a conflict between the Ninth and Sixth Circuits, because in *Pope v. Commissioner* we are confronted with a volume of sales which is substantially greater than in the instant case. As reported in the findings of fact and decision in the *Pope* case in 28 B. T. A., 1255, it appears that in the year 1925, 239 lots were sold; in 1926, 331½; the acreage subdivided was 222. The Court for the Sixth Circuit reversed the Board in its finding that the sales were not isolated transactions but represented continuity of effort. In the instant matter, the court held that the sales evidenced such continuity, there being 120 lots sold in 1934 and 186 in 1935, and 231 acres in subdivision. Thus in the Ninth Circuit a continuity of transactions sufficient to constitute a business is found on a lesser number of transactions than those which the Court for the Sixth Circuit held insufficient.

3. **The Circuit Court of Appeals for the Ninth Circuit erroneously concluded that notwithstanding the sales herein involved were only part of a liquidation forced upon petitioners, such sales were made in the ordinary course of their trade or business.**

It is to be remembered that petitioners did not subdivide the property, or any part thereof until after its acquisition at the foreclosure proceeding. The property which petitioners then recovered from the defaulted purchaser, the Ransom Corporation, had been plotted into subdivision, assessed as lots instead

of acres, with roads laid out, with improvement and other obligations against it, and which could be used for no other purpose than subdivision unless "they gave it away to somebody" (Record, page 109). Thus petitioners were compelled to set out on a liquidation of the property to salvage their interest in it. It is respectfully submitted that such liquidation is not the ordinary course of a taxpayer's trade or business within the meaning of section 117(b) of the Revenue Act of 1934.

This Court has in at least one analogous situation held that a liquidation of such character is not a business. This is necessarily the conclusion to be drawn from *Morrissey v. Commissioner,* 296 U. S. 344, 80 L. ed. 263, where, in determining the question whether a trust for the purpose of disposing of property constitutes an association taxable as a corporation, it was held that the association "was not a liquidating trust" and hence was not a business enterprise for profit.

VII.

CONCLUSION

Because the Circuit Court for the Ninth Circuit decided this case as it previously had others of similar character in direct conflict with the decisions in each of the Second and Sixth Circuits, and because there is herein presented an important question of Federal law which has not been but which should be settled by this Court, we respectfully urge that this petition be

granted. We ask that this Court hear this cause and determine the question whether the owner of investment property who, in liquidating it in the only manner practically feasible, disposes of it by way of subdivision, is engaged in that kind of business which is defined in section 117(b) of the Revenue Act of 1934 and similar provisions, as the sale of property held primarily for sale in the ordinary course of a taxpayer's trade or business.

Dated, San Francisco, California, August 28, 1941.

Respectfully submitted,

SIDNEY M. EHRMAN,
LLOYD W. DINKELSPIEL,
Counsel for Petitioners

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In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 577

FLORENCE H. EHRMAN, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

CLARA HELLMAN HELLER, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

FRANCES J. HELLMAN AND WELLS FARGO BANK & UNION TRUST CO., TRUSTEES UNDER THE LAST WILL AND TESTAMENT OF I. W. HELLMAN, JR., DECEASED, PETITIONERS

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 24–48) is reported in 41 B. T. A. 652. The

opinion of the Circuit Court of Appeals (R. 156-163) is reported in 120 F. (2d) 607.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on June 6, 1941 (R. 164). The petition for a writ of certiorari was filed September 2, 1941. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether gains realized by the petitioners from the subdivision of property owned by them and the sale of lots constituted ordinary income or capital gains under Section 117 (b) of the Revenue Act of 1934.

STATUTE INVOLVED

Revenue Act of 1934, 48 Stat. 680:

> SEC. 117. CAPITAL GAINS AND LOSSES.
>
> (a) *General Rule.*—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net income:
>
> * * * * *
>
> 30 per centum if the capital asset has been held for more than 10 years.
>
> (b) *Definition of Capital Assets.*—For the purposes of this title, "capital assets" means property held by the taxpayer

(whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business (U. S. C., Title 26, Sec. 101).

STATEMENT

The facts as found by the Board of Tax Appeals (R. 25–40) may be summarized as follows:

I. W. Hellman, Sr., was a banker. At his death in 1920 he left a considerable estate which included a large number of tracts of land, both improved and unimproved. This land included several ranch properties, one of which was Repetto Ranch, containing 1,569.93 acres and located about five miles east of the City Hall of Los Angeles, but outside the city limits. Repetto had been acquired by Hellman, Sr., between 1870 and 1880. It was used first for grazing and later, until 1929, for farming and horticulture (R. 26–27).

Upon the death of Hellman, Sr., the residue of his estate, including Repetto, passed in equal parts to his children. Two of the children and the trustee under the will of the third child are the petitioners here (R. 27).

No particular effort was made to sell Repetto prior to 1929. Offers were received and (except for two sales, totalling 8.5 acres) were rejected

by the petitioners, who were opposed to a subdivision project and wished to sell outright, either for cash or substantial cash and security for the balance. However, in 1929 about 800 acres of Repetto, constituting practically all of its level land, were sold to Ransom Corporation, which proposed to subdivide the land and sell it. The total consideration for the sale was $4,052,000, with a down payment of $250,000 cash, and the balance payable with interest over a period of approximately ten years. Title was conveyed to a bank, as trustee, under a declaration of trust (R. 27–29, 44, 72).

Ransom proceeded to develop a portion of the land, but in 1931 and 1932 became involved in difficulties. After negotiations the parties on May 16, 1932, entered into a modification of the declaration of trust, whereby all of the land except approximately 273 acres was released and the total purchase price reduced. Thereafter Ransom continued its efforts, but in a short time defaulted under the amended agreement, and on December 2, 1932, gave notice that it could no longer proceed. On July 31, 1933, the petitioners demanded sale and on February 13, 1934, purchased the property at trustee's sale, and deed was delivered to them on May 30, 1934 (R. 29–30).

The property so reacquired by the petitioners had been subdivided into lots, some of which had been deeded to purchasers and some of which were

under contracts of sale. The uncompleted contracts were acquired by the petitioners, as well as certain obligations, such as improvement and maintenance of the property and street and drainage district assessments. Prior to the trustee's sale petitioners' agent, Keller, investigated the situation at their request and advised that they carry on with the subdivision, first reducing the price of the lots to meet the market at that time. The Hamilton Sales Corporation was thereupon employed as agent of petitioners to carry on the work of the subdivision, and Hamilton started operations in November 1933, prior to the foreclosure.[1]

The first thing done was to restore to acreage parts of the land on which not many lots had been sold or contracted for sale. About 46 acres were so restored, and at about the same time, on November 9, 1933, a new tract of approximately 40 acres was opened by the petitioners for subdivision purposes, in order to centralize the entire subdivision and bring it closer to the business section (R. 30–32).

Two additional tracts were later added to the subdivision, one of 34.8 acres in 1937, and one of 64.8 acres in 1938, and subdivided by the peti-

[1] The contract between petitioners and Hamilton was entered into on February 19, 1934. It provided, in general, that Hamilton through its own sales organization was, for a commission, to sell the subdivided lots, subject to the direction of petitioners (R. 32–34; Pet. 6).

tioners. Shortly after Hamilton took over, the petitioners built and paid for five houses on the subdivision, for the purpose of promoting sales. Hamilton developed an active sales organization, including as many as 200 salesmen. Petitioners maintained and improved the subdivided property at their own cost, and contracted for public utility facilities for the subdivision as well as for improvement and maintenance, expending substantial sums for all these purposes (R. 34–35, 39).

Lot contracts and sales under the subdivision program were as follows (R. 36):

	Number of contracts, lots	Total sale price	Total payments made on contracts
1934	120	$161,679.87	$59,625.44
1935	186	230,170.00	105,276.70
1936	264	296,029.00	139,379.99
1937	258	342,565.00	230,465.88
1938	234	285,446.43	226,346.62

The petitioners returned the resulting income as capital gains and the Commissioner assessed deficiencies (R. 40, 20–22). The Board of Tax Appeals sustained his determination (R. 49–51). It found that the petitioners could have sold the whole ranch for a fair price and that they subdivided simply to obtain a better price (R. 44–45) and that the continuity and frequency of the sales showed that the property was held for a business sale (R. 47). The circuit court of appeals affirmed (R. 164).

ARGUMENT

1. Petitioners' argument seems to be that so-called "investment property" must retain that status and cannot become the subject of "business." But, even if property used for grazing and agriculture falls within petitioners' category of "investment property", section 117 (b) excludes from the capital gains provisions "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business." However acquired, the property after the inauguration of the subdivision program was obviously held for sale to customers in the ordinary course of that program. The assertion (Pet. 22) that subdivision was the only available means of sale is similarly irrelevant, and is in any event contradicted by the finding of the Board of Tax Appeals (R. 43–46).[2]

2. This is the fourth time that the court below has reached the same result upon parallel sets of facts. *Welch* v. *Solomon,* 99 F. (2d) 41 (C. C. A. 9); *Richards* v. *Commissioner,* 81 F. (2d) 369 (C. C. A. 9); *Commissioner* v. *Boeing,* 106 F. (2d) 305, certiorari denied, 308 U. S. 619. However, conflict is urged between the holding below and the

[2] The 1934 amendment, mentioned by petitioners (Pet. 23), adding the qualification that the sales must be "to customers" in the "ordinary" course of business, is irrelevant to sales such as these, and was designed only to include stock speculators within section 117. See H. Rpt. No. 1385, 73d Cong., 2d Sess., p. 22.

decisions in *Phipps* v. *Commissioner,* 54 F. (2d) 469 (C. C. A. 2), and *Pope* v. *Commissioner,* 77 F. (2d) 599 (C. C. A. 6). As shown by petitioners' quotations from *Phipps* v. *Commissioner* (Pet. 20), both the Second Circuit and the court below view the result as turning upon the continuity and the frequency of the sales, and the difference in result simply reflects the difference in the factual situations presented. In *Pope* v. *Commissioner, supra,* the court assumed that a real estate business was being conducted and merely held that the taxpayer, who was a stockholder and an inactive officer, was not engaged in the business of the corporation. The petition for a writ of certiorari in the *Boeing* case, which also claimed a conflict with the *Phipps* and *Pope* cases, was denied. While the asserted conflict did not receive the emphasis present counsel would have given it (Pet. 22), it was distinctly asserted (No. 511, October Term, 1939, Pet., pp. 11, 28) and was specifically answered in the brief in opposition (p. 11).

3. *Higgins* v. *Commissioner,* 312 U. S. 212, dealt with the question whether personal investment expenses were deductible as business expenses, and *Morrissey* v. *Commissioner,* 296 U. S. 344, with the question whether a trust was engaged in business. Apart from the dissimilarity in the facts of the cases, this Court has already recognized that the content of the definitions of doing business

necessarily varies in these diverse inquiries. *Higgins* v. *Commissioner, supra,* 217.

CONCLUSION

The decision below is correct and there is no conflict. It is, therefore, respectfully submitted that the petition should be denied.

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